

AUTO INSURANCE BUYER'S GUIDE

Introduction

Auto insurance is an expensive purchase for most Americans. This guide provides information to consumers on how to make decisions that can lower the cost of your auto insurance and increase the value you receive.

A National Association of Insurance Commissioners (NAIC) study found that in 1994 the average auto insurance premium expenditure for private passenger auto insurance was \$748 for each vehicle insured for one year. In many parts of the country, a year's auto insurance premium for a vehicle is measured in the thousands of dollars. What these figures show is that auto insurance is an important purchase for most American consumers.

To get the best buy for your money, you must take responsibility for your auto insurance purchase and make your own decisions.

Underwriting and Rating

Two factors determine what you pay for auto insurance. These factors analyze your characteristics and determine the risk that you present.

The first factor is underwriting. Insurance companies underwrite to assess the risk associated with an applicant, group the applicant with other similar risks and decide if the company will accept the application.

The second factor is rating. Based on the results of the underwriting process, the rating assigns a price based on what the insurer believes it will cost to assume the financial responsibility for the applicant's potential claim.

The purpose of underwriting is to sort applicants into groups of people that present similar risk and accept, deny or limit coverage for each group of applicants. What that means to you is that you will be grouped with other applicants and policyholders who have similar risk-related characteristics. Therefore, if you can lower your level of risk, you can be grouped with others with lower risk.

A rate for each group will be set based on the claims paid by the insurer for the people in that group. The higher the average losses from a group, the higher the rates for that group. Therefore, it is an advantage for you to be in a low-risk group.

How do insurers underwrite?

Insurers depend on information provided on your policy application. When you apply for insurance, you will be asked a series of questions. The purpose of these questions is to assess the likelihood of you filing a claim.

Insurers want to know your driving record. In addition, insurers want to know certain personal characteristics to group you with other drivers. Insurers review the claim history of your group to project future claims.

Some of these characteristics are beyond your control, such as age and gender. Other characteristics can be controlled but, since they may relate directly to lifestyle or income, may be difficult to control. These characteristics include geographic location and usage of the vehicle.

A third group is highly controllable and includes such characteristics as the make and model of your vehicle and your driving record. For example, a vehicle with few safety devices and a powerful engine carries a greater risk of high claims than other makes and models. You can choose to own and insure a car with less risk factors. Also, by choosing to drive safely and defensively, obeying speed limits and traffic signals, you can keep a good driving record or work to improve a less perfect record.

Insurers also consider life-style characteristics in the underwriting process. These characteristics include marital status and employment history. From prior claims data, insurers know that married persons tend to have lower claim levels than unmarried. Other statistics show that persons who work in the same place for a long time tend to have lower claims.

Rating

The second factor that governs the cost of your auto insurance is rating. Like underwriting guidelines, each company adopts its own rating system, although there are general guidelines that all companies follow.

Commonly asked questions insurers use for rating include:

- 1.) Driving Record: On the policy application you will be asked about your driving record. Insurers will ask about accidents and traffic violations for any driver covered by the policy for the preceding 3-5 years. Drivers with previous violations or at fault accidents are considered to be a higher risk and are charged a higher rate.
- 2.) Territory: The claims experience of people in your area will also affect your rates. Applications include a question that asks for the address where the vehicle will be garaged. From this information insurers can tell a great deal about your risk of financial loss. From prior claims experience, insurers know that more claims are made from urban areas than rural areas (busy traffic, thefts, vandalism, etc.).
- 3.) Gender and Age: Statistically, males still have more accidents than females. For this reason, men may tend to pay more for insurance than women. Insurers also have statistics that show a higher number of claims for some age groups than for others.
- 4.) Marital Status: Insurance company claims statistics show a lower rate of auto insurance claims among married policyholders.
- 5.) Prior Insurance Coverage: Insurers may ask you if you had insurance coverage previously. If you have previously been cancelled for non-payment of premiums, insurers want to know. If you have had insurance, your new insurer may ask your prior company about your claims history. Different insurance companies specialize in particular classes of business. Large insurers may form subsidiaries for preferred (low risk), standard and nonstandard (high risk) business.

6.) Vehicle Use: You will be asked on the application about how often and how far you drive the vehicle you want to insure. Higher use will generally result in higher premiums due to the higher exposure to risk.

7.) Make and Model of Vehicle: The type of car you drive will directly affect the cost of automobile insurance. A make or model of car that has a high number of claims or higher claims cost will be charged a higher premium for comprehensive and collision coverage.

The single greatest influence on the rating process is claim frequency. This does not mean how many times you specifically have made an insurance claim; although that will have an additional effect. Claim frequency measures how often an insured event occurs within a group relative to the number of policies contained in that group. Persons sharing characteristics with high-claims group will be charged more for insurance coverage. At the same time, persons who share characteristics with low claims classes will be charged lower rates. In addition, insurance companies offer discounts to individuals that exhibit certain characteristics.

Discounts

Discounts are awarded because the insurance company sees you as a "better risk". You should be aware of what discounts are offered by what companies before buying auto insurance. Not all states allow the same discounts to be used. Here are some discounts you should look for:

1.) Multiple Vehicles: Most insurance companies offer a discount to consumers that insure more than one car with their company. Companies offer these discounts not only because they want all of your business, but also because it is easier for them to underwrite individuals that they know; thus, reducing their risk and saving the company money. In addition, industry statistics show that individuals and families that insure more than one car have better than average claims experience. Through this discount, companies pass along some of their savings to you.

2.) Driver Education Courses: Discounts for driver education courses are targeted primarily at younger and older drivers.

3.) Good Student: Insurers have found that students who are responsible enough to earn a B average or better tend to be more responsible drivers. For that reason, many companies offer a good student discount.

4.) Safety Devices: Automobile safety devices can lower insurers' costs by preventing accidents or limiting their severity. These savings are passed along to the policyholder through discounts for safety equipment. This equipment includes: air bags, automatic seat belts and anti-lock brakes.

5.) Anti-theft Devices: Devices or systems that deter theft or vandalism also lower claims costs. Many companies offer discounts for anti-theft devices.

6.) Low Mileage: The fewer miles you drive the less chance you have of getting into an accident. Insurers recognize this fact and generally offer discounts for low mileage drivers. Some companies also offer discounts for drivers that participate in car-pools.

7.) Good Driver/Renewal: Some insurers offer discounts to drivers who maintain a good driving record and renew their policy with them.

8.) Auto/Home Package: Some insurers offer a discount on one or both policies if an individual buys a homeowner policy and an auto policy from the same insurer.

9.) Dividends: Some insurers, particularly mutual insurers, offer dividends to policyholders if the sale of auto insurance has been profitable to them. Dividends are declared and paid after the policy period has expired.

Discounts are not only ways for companies to attract customers, but they are also ways for companies to compete and retain business. So when you shop, do not just ask if a discount exists, but also ask how much you save. Savings can differ from company to company. In addition, you should make sure you receive the discounts for which you qualify. When comparing the price of insurance between different companies, compare the total cost after any discounts.

The Tort System

Insurance provides protection to consumers by assuming certain risks and promising to pay for financial losses. The type of insurance you buy will be based on how the financial loss can occur.

Tennessee operates under the Tort System. While you are not required to carry liability insurance in order to register your car or obtain a driver's license, it is strongly recommended that you purchase such coverage. Should you become subject to the Tennessee Financial Responsibility Statute due to an accident or a violation, you will be required to show proof of financial responsibility.

Liability Insurance

Most auto liability insurance policies contain three major parts: liability insurance for bodily injury, liability insurance for property damage, and uninsured/under-insured motorists coverage:

1.) Bodily injury liability insurance does not protect you or your car directly. If you cause an accident in which other people are injured, this insurance protects you against their claims for damages including medical expenses, lost wages and pain and suffering. This insurance coverage will also pay if the accident was caused by a member of your family living with you or a person using your car with your consent.

Bodily injury liability insurance carries specific benefit limits. These limits address how much money your insurance company is committed to pay for any one victim injured in an accident and limits the amount the company must pay for multiple victims.

To make a smart consumer purchase, you must understand these limits for bodily injury liability insurance. Minimum amounts are generally low and you may decide to purchase additional coverage. This decision may be based on your desire to protect your assets from additional claims above the minimum amounts. If this is the case, keep in mind that as you raise your coverage, your premiums will increase. This is because you are asking the insurance company to assume responsibility for a higher claim. The extra cost of higher coverage tends to be relatively low.

2.) Property damage liability insurance pays for any damage you cause to the property of others; such as a crushed fender, broken glass, or a damaged wall or fence. Your insurance will pay for this damage whether you are driving your automobile or whether it was being driven by another person with your consent. Once again, there will be maximum limits set by your policy on the claims your insurance company commits to pay as a result of property damage losses.

3.) Uninsured motorists coverage protects you directly. This coverage pays if you are injured by a hit-and-run driver or a driver who does not have auto insurance. This coverage, in effect, takes the place of the insurance that the other driver should have purchased but did not. Some policies

also contain coverage for under-insured drivers. These are driver who purchased insurance but not enough to cover your claim.

Once again, uninsured motorists coverage will have policy limits. Uninsured motorists coverage does not protect the other driver and it may not cover damage to your vehicle. Your insurance company may sue the other driver for any money the company pays to you because of the other driver's negligence.

The three coverages mentioned above are the basic coverages contained in liability policies sold under the Tort System. However, when you purchase auto insurance you will have to decide what other insurance coverages you would like to purchase.

Another way to provide higher limits of liability inexpensively is by purchasing a personal umbrella policy. An umbrella policy provides broad liability protection over and above your auto policy's liability limits. It will also cover some exposures to loss that are not covered by your auto or homeowner's policies.

Property Damage Coverage

The most commonly recognized coverages, in addition to the basic liability package outlined above, are collision and comprehensive coverages.

Collision coverage pays for physical damage to your car as the result of your auto colliding with an object, such as a tree or another car. This is relatively expensive coverage. Remember, this coverage is optional and not required by law. However, collision insurance may be required by your lending institution or lessor.

If you have an older vehicle worth less than \$2,000, there is little reason for you to purchase collision coverage because you are likely to pay more money in premium than you would ever receive as a result of a claim. Auto insurance policies only require the company to cover your financial expenses, not to replace your vehicle. In the case of an accident involving an older car, the cost of repairing the car can quickly exceed the worth of the car. In that case, insurers will "total" the car and pay you what the car was worth rather than fixing it. In severe cases, the worth of the car may not exceed the premiums paid for the coverages.

1.) Comprehensive coverage pays for damage to your auto from almost all other causes, including: fire, severe weather, vandalism, floods and theft. Comprehensive coverage will also cover broken glass, such as windshield damage. Comprehensive coverage is less expensive than collision coverage and many consumers choose to carry it. However, remember it is your choice; you are not required by law to carry comprehensive coverage.

When considering collision and comprehensive coverage, you should consider your deductible. A deductible is an amount of money you agree to pay as part of a claim before the insurer is committed to pay the rest of the claim. For example, if you carried collision coverage with a \$200 deductible and you had a \$500 loss, you would have to pay \$200 and the insurance company would have to pay the remaining \$300.

Basically, deductibles reduce your premiums because you agree to deduct a set amount from the claim your insurer otherwise would have to pay. Insurance companies offer deductibles because they reduce the number of small claims which are costly for them to handle.

If you purchase a new car with a loan, the financial institution that lent you the money may require you to purchase collision coverage. This is because they see your car as collateral for the loan, and they want to make certain it is worth something if they need to repossess it.

In the event you have to buy, or decide to buy, collision or comprehensive coverage, you can save money by agreeing to the highest deductible you can afford to pay in the event of an accident. However, since comprehensive coverage is usually cheaper than collision coverage, many people save money by dropping the collision coverage and keeping the comprehensive coverage to protect against natural perils, theft and glass breakage.

Other Optional Coverages

Be cautious when purchasing these coverages. They can duplicate coverage that you may pay for through other insurance policies. For instance, medical payments coverage may duplicate health or disability benefits that you buy individually or receive as a benefit through your job. Before purchasing these coverages, review them and your other insurance policies carefully.

1.) Medical payments coverage is one such optional coverage. This coverage pays for the medical and funeral expenses for you or others injured or killed in an accident while riding or driving in your auto. Claims against this coverage include all reasonable hospital, surgical, chiropractor, X-ray, dental, professional nursing, prosthetic and funeral expenses. It will also cover you or members of your family if you are struck by an auto while walking or riding in another auto. This coverage will also pay for your medical and funeral expenses even if you cause the accident. Usually, only expenses incurred within a specified period of time after the accident are included.

2.) Rental reimbursement coverage usually pays \$15 to \$20 a day to rent a car for a specific number of days while your vehicle is being repaired. The premium will vary from insurer to insurer.

3.) Towing and labor coverage pays the cost of towing your car to the repair shop subject to the limit of your policy. Premium for this coverage can run as low as \$5 to \$10 per year. However, if you are a member of an auto club, you probably already have this service and may not want to duplicate your coverage.

Smart Shopping

The key to comparison shopping is to know what insurance coverages you need before you start and then to find out how much those coverages will cost from a number of companies. Comparison shopping takes time but will save you money. Different companies charge different rates for the same coverage.

No one wants to pay more for their auto insurance than they absolutely have to. The only way you can make certain you are not paying too much is to shop around. Find out what different companies charge for identical products and services.

Seek Unbiased Information

Information is available to consumers from a number of unbiased sources. In addition to the information provided by this department, these sources include: public libraries, various consumer groups and consumer publications.

The insurance industry, like many other industries, has developed many words not commonly used by the average person. Consumers may need to find a good glossary or dictionary of insurance terms from the public library.

Where to Shop

When you begin to contact companies, there are a few things you should know about how insurance companies sell insurance.

Most insurance companies and many agents advertise. Check the newspaper and yellow pages of the telephone directory for companies and agents in your area. In addition, contact your neighbors, relatives and friends for recommendations on insurance companies and agents. Ask them about their experience regarding price and service. In particular ask them what kind of claim service they have received from the companies they recommend.

Consumers often rely on their insurance agent or company to tell them what kind of coverage they need. Insurance agents are paid on a commission basis, which means the higher the premium, the more money they make. The commission system of agent compensation is a strong incentive for higher premiums. Certainly, competition between agents for business provides some incentive to push down rates lower than other agents but not necessarily the lowest price possible. If consumers want the lowest price possible, they must take responsibility for finding it themselves. Remember, competition only works if the consumer shops for coverage.

Price Quotations

When shopping for auto insurance, premium quotations are a useful tool for comparison of different companies' products. When asking for price quotations, it is crucial that you provide the same information to each agent or company.

To give you an accurate quote the agent or company will usually request the following information:

- * A description of your vehicle
- * Its use
- * Your drivers license number
- * The number of drivers in your household
- * The coverages
- * The limits you want
- * Accidents/Tickets for last 3-5 years

This information is necessary to the rating process described earlier in this guide.

Insurance Marketing Methods

You should understand that not all insurance companies use insurance agents to sell their product. Insurance companies generally use one of three methods to market their product: direct

marketing, independent agents or exclusive agents. The type of marketing method may be good or bad for a consumer, depending on the type of services offered. Therefore, consumers should be aware of each of the three methods and may want to consider them in their purchase decision.

Direct marketers sell insurance through the mail and by telephone. In some cases, consumers can save money with direct marketers because these companies do not have to pay insurance agents commissions to sell their policies. Companies can pass along this savings to the consumer. However, some consumers prefer to pay an additional premium for the opportunity to have a local agent available to them.

If you decide to call an agent for quotations, ask them how many companies they represent. Independent agents represent several companies, therefore, you can get quotes for more than one company from one agent. This is considered an advantage to many consumers.

If you contact an independent agent, be aware that the companies the agent represents are in competition with one another for business. In an effort to encourage the agent to sell their product, companies may compete by offering higher commissions and incentives to the agent. As a result, insurance companies that use independent agents may have to charge a little extra in order to pay the agent higher commissions. However, this is not always the case.

Some insurance companies sell coverage through agents that only represent their company. These companies call their agents an exclusive agency force. Exclusive agents can only offer you coverage from the company they represent; therefore, you can only get a quote from one company for each exclusive agent that you talk to.

Sometimes exclusive agents may work for a lower rate of commission than independent agents. This is because companies do not have to give the agent an incentive to write their product over another company's product. The lower commission structure, especially on commissions for renewal business, can represent significant cost savings to the insurance company and often a portion of that savings is passed along to the consumer in lower premiums.

When considering the purchase of an insurance product from an insurance agent, it is advisable to ask what rate of commission the agent is being paid for the sale of the policy. This is not an unfair or personal question. After all, you are paying the commission with your premium dollars.

For Your Protection

Once you have selected the insurance coverages you need and an insurance agent or company, there are steps you can take to make certain you get your money's worth.

Before signing an application for any insurance coverage, call Agent's Licensing at 1-888-416-0868 and verify that the company and the agent you are dealing with are licensed in Tennessee. It is illegal for unlicensed insurers to sell insurance. Business cards are not proof of a licensed insurance agent or company. If you do business with an unlicensed agent or company, you have no guarantee that the coverage you pay for will ever be honored. If you purchase insurance from companies not legally doing business in Tennessee, you may not be protected by the guaranty fund should the company fail.

If you are contacted by an unlicensed insurance agent or company, call Consumer Insurance Services at 1-800-342-4029, immediately, so that regulatory action can be taken. By doing so, you may protect someone less knowledgeable than yourself from being victimized.

You should be aware that an auto insurance policy is a legal contract. It is written so that your rights and responsibilities as well as those of the insurance company are clearly stated. When you purchase auto insurance, you will receive a policy. You should read that policy and make certain you understand its contents. If you have questions about your insurance policy, contact your insurance agent for clarification. If you still have questions, contact Consumer Insurance Services at 1-800-342-4029.

The Tennessee Department of Commerce & Insurance is here to serve the consumers of Tennessee. Our Insurance Division can be a source of unbiased information and assistance to you when shopping for your insurance needs.

If you have a complaint against an insurer, it is always best to contact your insurance company first to attempt to settle the matter. Most insurance companies have policyholder service offices set up precisely to handle such questions. If you still are not satisfied, contact this department. We have complaint investigators in our Consumer Insurance Services section to assist you with your concerns. Although they cannot represent you legally against an insurance company or adjuster, they can make appropriate investigation into potential violations of insurance laws or regulations based upon your complaint.

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